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SC PUBLIC SERVICE
COMMISSION

February 22, 2005

Mr. Charles L.A. Terreni
Chief Clerk/Administrator
South Carolina Public Service Commission
101 Executive Center Dr., Suite 100
Columbia, SC 29210

Re: Application of Midlands Utility, Inc. for an approval of New Schedule of Rates and Charges for Sewage Service provided to its customers in Richland, Lexington, Fairfield and Orangeburg Counties.
PSC Docket No.: 2004-297-S

Dear Charles:

Enclosed for filing please find the original and twenty-six (26) copies of the Surrebuttal Testimony of the following Office of Regulatory Staff Witnesses: Willie J. Morgan, Dawn M. Hipp and Roy H. Barnette in the above referenced matter. Please date stamp the extra copy enclosed and return it to me via our courier.

Please let me know if you have any questions.

Sincerely,

Wendy B. Cartledge

Wendy B. Cartledge

WBC/cc

Enclosures

cc: Charles Cook, Esquire

BEFORE
THE PUBLIC SERVICE COMMISSION
OF SOUTH CAROLINA
DOCKET NO. 2004-297-S

IN RE: Application of MIDLANDS)
UTILITIES, INC. for an Approval)
Of New Schedule of Rates and)
Charges For Sewage Service)
Provided to its Customers in)
Richland, Lexington, Fairfield and)
Orangeburg Counties.)
_____)

CERTIFICATE OF SERVICE

This is to certify that I, Cindy Clary, an employee with the Office of Regulatory Staff, have this date served one (1) copy of the Surrebuttal Testimony of Willie J. Morgan, Dawn M. Hipp and Roy H. Barnette in the above-referenced matter to the person(s) named below by causing said copy to be deposited in the United States Postal Service, first class postage prepaid and affixed thereto, and addressed as shown below:

Charles Cook, Esquire
Elliott & Elliott, P.A.
721 Olive Street
Columbia, South Carolina 29205



Cindy Clary

February 22, 2005
Columbia, South Carolina

172822

SURREBUTTAL TESTIMONY OF ROY H. BARNETTE
FOR
THE OFFICE OF REGULATORY STAFF
DOCKET NO. 2004-297-S
IN RE: MIDLANDS UTILITY, INC.

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Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION.

A. My name is Roy H. Barnette. My business address is 1441 Main Street, Suite 300, Columbia, South Carolina. I am employed by the Office of Regulatory Staff ("ORS") as an Auditor.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY INVOLVING MIDLANDS UTILITY, INC. ("MUI")?

A. The purpose of my surrebuttal testimony is to address and explain the issues brought forth by the Company in its rebuttal testimony.

Q. PLEASE EXPLAIN YOUR DISALLOWANCE OF CERTAIN EXPENSES BECAUSE THEY WERE NOT KNOWN AND MEASURABLE.

A. During the performance of the audit, ORS requested copies of invoices or other evidence to support the per book numbers. The MUI staff was most helpful in fulfilling these requests; however, in the case of items on a going forward basis, the company was not able to provide documentation, i.e., purchase orders, etc., to support the dollar amounts included in its application. Therefore, ORS determined

1 these costs not to be known and measurable, thus unallowable for rate making
2 purposes.

3 **Q. PLEASE EXPLAIN THE NEED FOR RECLASSIFICATION OR**
4 **ALLOCATION ADJUSTMENTS DURING THE AUDIT.**

5 A. During the performance of the audit, ORS determined that several items had been
6 expensed to an incorrect account or paid for by one of the affiliated companies and
7 not properly recorded on the books of the other affiliates. Therefore, it was necessary
8 for ORS to reclassify certain expenses and allocate other expenses between the three
9 companies. As stated in my prefiled testimony, ORS recommends that the affiliated
10 companies of DSI, BRUI and MUI merge their operations and consolidate their
11 books and records considering they share common ownership, purpose, staffing,
12 inter-company borrowing of assets, expenses and equipment. If a merger of the
13 companies occurs, allocations would no longer be necessary, and the company's
14 record keeping procedures would be simplified.

15 **Q. WHY DID THE ORS DISALLOW THE COMPANY'S PROPOSED**
16 **INCREASE IN OFFICER'S SALARIES OF \$19,808?**

17 A. During the examination of the Company, the financial records revealed no increases
18 had been granted and no accruals recorded for officers' salaries were included.
19 Therefore, their proposed adjustment was disallowed.

20 **Q. PLEASE DISCUSS ADJUSTMENT #5 AS IT RELATES TO A REDUCTION**
21 **IN ALLOWABLE EXPENSES IN THE AMOUNT OF \$16,692?**

22 A. During the course of the audit it was determined that several items which had been
23 expensed should have been capitalized. These items were not disallowed but were

1 merely reclassified as capital investment in accordance with generally accepted
2 accounting principals. The items in questions are included on Audit Exhibit A-2,
3 show purchase dates of August 2003 – May 2004, and are being depreciated.

4 **Q. PLEASE DISCUSS THE DISALLOWANCE OF THE COMPANY'S**
5 **PROPOSED ADJUSTMENT OF \$27,120 IN O&M EXPENSES – SERVICE**
6 **CONTRACTS (DSI)?**

7 A. During the DSI rate case, DSI proposed to increase its revenues as a result of a
8 correction made by DSI to reflect the appropriate level of treatment expenses. DSI
9 proposed to charge MUI, \$27,120 for the use of DSI's equipment. No contract was
10 issued and therefore the adjustment was determined by ORS to be unallowable.
11 Subsequently, the Commission in Docket No. 2004-212-S, Order No. 2005-42 dated
12 February 2, 2005, agreed with the ORS staff in its determination. Furthermore, ORS
13 noted no Account Payable in the books and records of MUI and therefore disallowed
14 the proposed adjustment.

15 **Q. WHY DID THE ORS DISALLOW \$47,464 IN LEGAL AND PROFESSIONAL**
16 **FEES?**

17 A. During the course of the audit the ORS identified certain expenses included in Legal
18 and Professional fees which it determined to be unallowable. The \$47,646 that was
19 disallowed by the ORS was comprised of \$19,415 for lobbying, which can not be
20 considered as an allowable expense in ratemaking, \$666 related to the filing of the
21 loan documents, an expense that should be capitalized and depreciated over the
22 useful life of the asset and \$27,383 in payments for services received outside the test
23 year.

1 **Q. PLEASE DISCUSS ADJUSTMENT #33 AS IT PERTAINS TO MR. KEITH**
2 **PARNELL'S ASSUMPTION THAT THE ORS PROPOSES AN**
3 **ADJUSTMENT OF \$32,756 TO INTEREST EXPENSE?**

4 A. The ORS does not propose an adjustment to Interest Expense of \$32,756. MUI
5 proposes an adjustment of this amount. ORS's proposed interest adjustment in this
6 entry is \$238. (Please refer to Audit Exhibit A-1, Page 4 of 5, Adjustment #33 for
7 clarification). The adjustment states that "MUI proposes an adjustment to Interest
8 Expense of \$32,756." Though not stated in direct testimony, the ORS would be
9 opposed to the company's adjustment of \$32,756; this interest is construction period
10 interest and should be capitalized in accordance with generally accepted accounting
11 principles.

12 **Q. PLEASE DISCUSS ORS'S RELIANCE ON NARUC AND OTHER**
13 **GUIDELINES.**

14 A. The ORS uses several sources of accounting theory and practice on which to base its
15 findings and recommendations. Those include NARUC, previous Commission orders
16 and generally accepted accounting principles (GAAP). ORS acknowledges that none
17 of these guidelines constitute law; however, they do comprise accepted regulatory
18 principles. Also, it should be noted that the use of NARUC guidelines by sewer
19 utilities is required by law (26 S.C. Code Regs. 103-517).

20 The ORS would like to commend the staff of MUI for its recent decision to convert
21 to the NARUC chart of accounts and wish them well in the conversion process.

22 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

23 A. Yes, it does.